

Stone Harbor Emerging Markets Income Fund
Form N-CSRS
August 05, 2011
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM N-CSR

CERTIFIED SHAREHOLDER REPORT OF REGISTERED

MANAGEMENT INVESTMENT COMPANIES

Investment Company Act file number: 811-22473

Stone Harbor Emerging Markets Income Fund

(Exact name of registrant as specified in charter)

1290 Broadway, Suite 1100

Denver, CO 80203

(Address of principal executive offices) (Zip code)

Adam J. Shapiro, Esq.

c/o Stone Harbor Investment Partners LP

31 West 52nd Street, 16th Floor

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(Name and address of agent for service)

With copies To:

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Date of fiscal year end: November 30

Date of reporting period: December 22, 2010 May 31, 2011

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Item 1. **Report to Stockholders.**

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Trustees & Officers

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Stone Harbor Emerging Markets Income Fund

Shareholder Letter

May 31, 2011 (Unaudited)

Dear Shareholder:

We appreciate your confidence in Stone Harbor Investment Partners, the investment manager of the Stone Harbor Emerging Markets Income Fund. As you know, the Fund's objective is to maximize total return, which consists of income on its investments and capital appreciation. The Fund invests primarily in debt securities issued by governments and corporations in emerging market countries. The investments are denominated in both U.S. dollars and in local currencies.

We believe that the continuing trends of credit improvement and strong economic growth make emerging market debt investments very attractive versus bonds from developed countries. We believe that these fundamentals, coupled with Stone Harbor's many years of experience in the asset class, put us in a good position to achieve the Fund's objectives. At Stone Harbor we endeavor to keep you well informed. Please feel free to call us at 877-206-0791 if you have any questions about your investment in our Fund.

Performance Review

Emerging Markets Debt Fund investors fared well in the Fund's initial reporting period. The total return on net asset value (NAV) of the Fund from inception of December 23, 2010 to May 31, 2011 was 7.32%. This performance compared quite favorably to most comparable indices for the period (See Figure 1). On a market value basis, the Fund's total return was 3.08% during this period.

Figure 1. Comparative Asset Class/Index Returns, 23 December 2010 to 31 May 2011

Energy Commodities	12.59%
Gold	11.12%
Broad Commodities	9.07%
EM Local Currency Debt	8.09%
S&P 500	7.92%
EDF (NAV)	7.32%
US High Yield Bonds	6.28%
Barclays Global Aggregate (Fixed Income)	6.26%
US TIPS	5.42%
US Investment Grade Debt	4.87%
US Treasuries 7-10 Year	4.78%
EM Equities	4.73%
EM Corporate Debt, High Yield	4.60%
EM External Sovereign Debt	4.02%
EM Corporate Debt	3.83%
EM Corporate Debt, Investment Grade	3.46%
Agricultural Commodities	1.95%
US Dollar	-7.31%

Source: Bloomberg, Stone Harborⁱ

For the reporting period, EDF's NAV outperformed its benchmark, the JP Morgan Emerging Market Bond Index - Global Diversified, by 3.30%. Most of this excess return resulted from security selection decisions in external sovereign debt and local currency bonds. Local currencies benefitted largely from a declining US dollar, but also from continuing strength in many key emerging markets (EM) economies. On balance, our country selection decisions detracted from performance, but our allocations to corporate debt in most countries enhanced total return relative to the index. We actively manage the allocations to external sovereign (US dollar-denominated), corporate, and local currency debt, based on the intensive credit research and relative value analysis of our portfolio management and research teams. On May 31, 2011, EDF's allocations were 50.1% local currency sovereign debt, 30.5% external sovereign debt, 19.3% corporate debt and 0.1% net cash.

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Market Review

We are particularly pleased with the performance of the Fund given the market headwinds that global investors faced during the period. While not an exhaustive list, the potentially destabilizing events during the period included:

1. The governments of Egypt and Tunisia were toppled by popular insurrection
2. The war began in Libya
3. Oil prices (Brent crude) climbed to a peak of \$126.74, nearly 35% higher than when EDF was launched
4. Japan's tsunami and earthquake resulted in significant economic destruction, particularly in global supply chains.
5. The sovereign debt crisis in Europe's periphery intensified; Portugal, Greece and Ireland were downgraded.
6. The US Federal Reserve ended the second round of quantitative easing, dubbed QE2.
7. The US economy entered a lull in growth in the second quarter, raising worries of the potential for a double-dip recession

Despite rising geopolitical and macroeconomic risks in the developed world, the fundamental characteristics of most EMs—fast growth rates, relatively low debt levels and improved policy making in both fiscal and monetary matters—remained supportive of the EM debt asset classes. EM growth rates remained well above growth rates of developed countries. Commodity prices stabilized, but remained at relatively high levels, fueled largely by EM demand. Since many EM countries are rich in natural resources, the sustained high level of commodity prices has enriched EM exporters and provided a steady stream of new cash flow, all of which supported EM governments' and companies' abilities to repay their debts. EM central banks continued normalizing monetary policy during the reporting period, hiking short term policy rates or raising bank reserve requirement ratios to cool inflation pressures. We expect more EM central banks to allow currency appreciation in the months ahead to help in an effort to stave off the threat of inflation.

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Stone Harbor Emerging Markets Income Fund

Shareholder Letter

May 31, 2011 (Unaudited)

Our strategy focused on investing in assets with attractive total return potential from EM countries and companies of improving credit quality. At the end of the period our allocations reflected our strong bias in favor of local currency and corporate bonds from many fast growing EM countries. In addition, we held exposure to select sovereign external bonds where we saw strong valuations and potential for return from spread compression.

Our outlook for the remainder of the year remains constructive for EM debt. While signs of a global soft patch in economic activity have affected EM economies as industrial production figures have weakened recently, growth rates have remained solidly positive in most EMs; we believe EM growth rates will continue to outpace developed country growth rates this year. While policy rates in core developed countries may begin to normalize by year end, interest rates are most likely to remain very low, in our opinion. Inflation pressures, as we see it, have been eased in part by prudent monetary policies of many EM central banks, but also by the stabilization of commodity prices in recent months. Moreover, continued institutional investments in EM debt, which reflect a shift to strategic allocations to the asset class, provide further strong support.

Nevertheless, we recognize several specific market risks to our benign base case, including:

1. Europe fails to provide a comprehensive solution to the sovereign debt crises in Portugal, Italy, Ireland, Greece and Spain
2. The US economy slips back into recession
3. China's economy weakens, producing a hard landing of sub 7% annual growth rate
4. EM policy makers engage in trade wars in an effort to counteract the economic effects of a falling US dollar
5. EM central banks fall behind in their efforts to curb inflation
6. US interest rates rise sharply reflecting rising fiscal deficits and the end of quantitative easing.

Other general risks of the Fund relate to our use of leverage and also to the longer-term prospects for a rise in global interest rates. With respect to leverage, Stone Harbor tactically employs leverage to enhance returns. During the performance period, leverage consisted primarily of borrowings using short term reverse repurchase agreements through which the Fund loans securities with the obligation to repurchase them at a later date at a fixed price. The implied borrowing costs of the repurchase agreements averaged approximately 0.56% per annum. The level of gross leverage was increased to a maximum of 24.4% of total assets in February, but was reduced by the end of the period to 17.96%. The Fund management team varied borrowing levels to reflect the team's outlook on the EM debt markets. The team increased borrowings when it felt opportunities had increased and reduced borrowings when, in the team's judgment, macroeconomic risks had risen. The Fund's lower level of gross leverage at the end of the period reflected the team's assessment of the rising risks of a sovereign default in Europe's southern periphery as well as a slow

down in US growth. Nevertheless, the Fund's allocations express a positive secular outlook for emerging markets.

As it pertains to the risk of a general rise in global interest rates, Stone Harbor attempts to mitigate the risk of loss of principal through its allocation process. We seek to upgrade credit quality and reduce duration exposure during periods of rising rates. Notwithstanding these efforts, rising interest rates would increase the Fund's cost of leverage and could also decrease the value of its portfolio securities, adversely affecting fund performance.

Notwithstanding these risks, we anticipate further strong gains from EM debt through the remainder of 2011 and continue to believe that all three sectors of the asset class - external sovereign, corporate and local currency debt - offer attractive risk-adjusted returns for investors.

Once again, we thank you for choosing Stone Harbor Investment Partners.

Sincerely,

Thomas W. Brock
Chairman of the Board of Trustees

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List of indices

CEMBI Broad Diversified High Grade

CEMBI Broad Diversified High Yield

CEMBI Broad Diversified

GBI EM Global Diversified

EMBI Global Diversified

Citigroup High Yield Capped

JP Morgan U.S. High Grade

S&P GSCI Energy

S&P GSCI Agriculture

SPDR Gold Trust

Barclays U.S. TIPS

Barclays U.S. Treasury 7-10 Year

Barclays Global Aggregate

MSCI Emerging Markets Free

S&P 500 Index

U.S. Dollar Index

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Stone Harbor Emerging Markets Income Fund

Summary of Portfolio Holdings

May 31, 2011 (Unaudited)

Under SEC Rules, all funds are required to include in their annual and semi-annual shareholder reports a presentation of portfolio holdings in a table, chart or graph by reasonably identifiable categories. The following tables, which present holdings as a percent of total net assets (TNA), are provided in compliance with such requirements.

STONE HARBOR EMERGING MARKETS INCOME FUND

Country Breakdown	% of TNA
Argentina	16.29%
Brazil	15.46%
Mexico	14.86%
Venezuela	11.49%
Indonesia	10.64%
South Africa	9.90%
Ukraine	9.54%
Iraq	5.95%
Colombia	4.77%
Turkey	2.33%
Kazakhstan	2.11%
Malaysia	1.98%
Russia	1.65%
Poland	1.43%
United Arab Emirates	1.18%
Dominican Republic	1.08%
China	1.05%
Luxembourg	0.90%
Peru	0.80%
Croatia	0.69%
Philippines	0.48%
India	0.40%
Egypt	0.30%
Ghana	0.18%
Uruguay	0.13%
Total	115.59%
Money Market Mutual Funds	6.92%
Liabilities in Excess of Other Assets	-22.51%
Total Net Assets	100.00%

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Stone Harbor Emerging Markets Income Fund

Summary of Portfolio Holdings

May 31, 2011 (Unaudited)

Security Type Allocation***Sector Allocation***

Sovereign Local	50.1%
Sovereign Dollar	30.5%
Corporate	19.3%
Net Cash	0.1%

Regional Breakdown*

Latin America	54.8%
Europe	18.3%
Asia	12.2%
Africa	8.7%
Middle East	5.9%
Net Cash	0.1%

Currency Breakdown*

Argentine Peso	4.70%
Brazilian Real	10.80%
Colombian Peso	4.00%
Indonesian Rupiah	5.40%
Mexican Peso	9.60%
Malaysian Ringgit	1.60%
Philippine Peso	0.40%
Polish Zloty	1.20%
Russian Ruble	2.70%
Turkish Lira	1.50%
South African Rand	8.20%
United States Dollar	49.90%
Total	100.00%

* Based on managed assets including derivative exposure. For purposes of this example, managed assets are defined as total net assets plus any borrowings attributed to the use of reverse repurchase agreements.

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Stone Harbor Emerging Markets Income Fund

Growth of \$10,000 Investment
May 31, 2011 (Unaudited)

Comparison of Change in Value of \$10,000 Investment in Stone Harbor Emerging Markets Income Fund and the JP Morgan Emerging Market Bond Global Diversified Index.

The JP Morgan Emerging Market Bond Global Diversified Index is a uniquely-weighted version of the EMBI Global Index, which tracks total returns for U.S. dollar-denominated debt instruments issued by emerging market sovereign and quasi-sovereign entities such as Brady bonds, loans and Eurobonds. Currently, the EMBI Global Index covers 196 instruments across 28 countries. It limits the weights of those index countries with larger debt stocks by only including specified portions of these countries' eligible debt outstanding. The countries covered in the EMBI Global Diversified are identical to those covered by the EMBI Global Index.

Average Annual Total Returns as of May 31, 2011

	3 Months	Since Inception	Inception Date
Stone Harbor Emerging Markets Income Fund - NAV	8.50%	7.32%	12/22/10
Stone Harbor Emerging Markets Income Fund Market Price	4.12%	3.08%	
JP Morgan EMBI Global Diversified Index	4.14%	4.11%	

Past performance is no guarantee of future results. Current performance may be lower or higher than the performance shown. Total return is calculated by determining the percentage change in NAV or market price (as applicable) in the specified period. The calculation assumes that all income dividends, capital gain and return of capital distributions, if any, have been reinvested and includes all fee waivers and expense reimbursements. Total return does not reflect the deduction of taxes that a shareholder would pay on Fund distributions or broker commissions or sales charges in connection with the purchase or sale of Fund shares. Investment return and principal value will vary, and shares, when sold, may be worth more or less than their original cost. Total returns for a period of less than one year are not annualized. Index returns do not include the effects of sales charges or management fees. It is not possible to invest directly in an index.

Performance at market price will differ from its results at NAV. Although market price returns typically reflect investment results over time, during shorter periods returns at market price can also be influenced by factors such as changing views about the Fund, market conditions, supply and demand for the Fund's shares, or changes in Fund dividends.

An investment in the Fund involves risk, including the loss of principal. Total return, market price, market price yield and NAV will fluctuate with changes in market conditions. This data is provided for information purposes only and is not intended for trading purposes. Closed-end funds, unlike open-end funds, are not continuously offered. There is a onetime public offering and once issued, shares of closed-end funds are traded in the open market through a stock exchange. NAV is equal to total assets attributable to common shareholders less total liabilities divided by the number of common shares outstanding. Holdings are subject to change daily.

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Stone Harbor Emerging Markets Income Fund

Statement of Investments

May 31, 2011 (Unaudited)

	Currency	Rate	Maturity Date	Principal Amount *	Market Value (Expressed in U.S. \$)
SOVEREIGN DEBT OBLIGATIONS - 50.47%					
Argentina - 13.84%					
<i>Republic of Argentina:</i>					
	ARS	2.000%	09/30/2014	\$ 15,745,013	\$ 3,525,869 ⁽¹⁾⁽²⁾
		7.000%	04/17/2017	18,398,523	16,642,486 ⁽³⁾
		8.280%	12/31/2033	10,859,924	9,339,535 ⁽³⁾
	ARS	5.820%	12/31/2033	54,820,730	17,933,792 ⁽¹⁾⁽²⁾
		0.000%	12/15/2035	1,554,684	256,911 ⁽¹⁾
	EUR	0.000%	12/15/2035	25,889,000	5,262,522 ⁽¹⁾
					52,961,115
Colombia - 0.28%					
<i>Republic of Colombia</i>					
		7.375%	09/18/2037	857,000	1,081,963
Croatia - 0.69%					
<i>Croatian Government</i>					
		6.375%	03/24/2021	2,560,000	2,644,480 ⁽⁴⁾
Ghana - 0.18%					
<i>Republic of Ghana</i>					
		8.500%	10/04/2017	596,000	669,755 ⁽⁵⁾
Iraq - 1.33%					
<i>Republic of Iraq</i>					
		5.800%	01/15/2028	5,500,000	5,080,625 ⁽⁵⁾
Malaysia - 1.98%					
<i>Malaysian Government:</i>					
	MYR	5.094%	04/30/2014	16,380,000	5,705,164
	MYR	4.012%	09/15/2017	5,500,000	1,851,146
					7,556,310
Mexico - 11.30%					
<i>Mexican Bonos:</i>					
	MXN	8.000%	06/11/2020	283,700,000	26,562,253
	MXN	8.500%	05/31/2029	175,700,000	16,666,585
					43,228,838
Philippines - 0.48%					
<i>Republic of Philippines</i>					
	PHP	4.950%	01/15/2021	79,000,000	1,844,429
Poland - 1.43%					
<i>Republic of Poland</i>					
	PLN	5.500%	04/25/2015	15,000,000	5,484,491

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Russia - 1.65%

<i>Russian Federation</i>	7.500%	03/31/2030	5,362,965	6,322,936 ⁽³⁾⁽⁵⁾⁽⁶⁾
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See Notes to Financial Statements.

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Stone Harbor Emerging Markets Income Fund

Statement of Investments

May 31, 2011 (Unaudited)

					Market Value
					(Expressed
	Currency	Rate	Maturity Date	Principal Amount *	in U.S. \$)
South Africa - 9.90%					
<i>Republic of South Africa:</i>					
	ZAR	8.250%	09/15/2017	\$ 70,000,000	\$ 10,372,223
	ZAR	8.000%	12/21/2018	12,940,000	1,879,021
		6.875%	05/27/2019	570,000	678,870
	ZAR	7.250%	01/15/2020	6,840,000	941,909
	ZAR	6.750%	03/31/2021	92,540,000	12,168,358
	ZAR	10.500%	12/21/2026	69,020,000	11,861,111
					37,901,492
Turkey - 1.79%					
<i>Republic of Turkey</i>					
	TRY	10.000%	02/15/2012	10,305,450	6,860,829
Ukraine - 3.07%					
<i>Ukraine Government:</i>					
		7.650%	06/11/2013	7,183,000	7,631,937 ⁽³⁾⁽⁵⁾
		6.875%	09/23/2015	2,000,000	2,075,000 ⁽⁴⁾
		7.750%	09/23/2020	2,000,000	2,053,000 ⁽³⁾⁽⁵⁾
					11,759,937
Uruguay - 0.13%					
<i>Republic of Uruguay</i>					
		9.250%	05/17/2017	385,000	503,388
Venezuela - 2.42%					
<i>Republic of Venezuela</i>					
		12.750%	08/23/2022	10,773,600	9,265,296 ⁽³⁾⁽⁵⁾
TOTAL SOVEREIGN DEBT OBLIGATIONS					193,165,884
(Amortized Cost \$189,985,999)					
BANK LOANS - 3.89%⁽⁷⁾					
Brazil - 0.52%					
<i>Virgolino de Oliveira - GVO Loan</i>					
		5.273%	03/11/2015	2,000,000	2,000,000
Indonesia - 3.37%					
<i>PT Bumi Tranche A</i>					
		0.000%	03/02/2012	7,157,442	7,157,442 ⁽²⁾
<i>PT Bumi Tranche B</i>					
		0.000%	03/02/2012	5,712,558	5,712,558 ⁽²⁾
					12,870,000

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TOTAL BANK LOANS	14,870,000
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(Amortized Cost \$14,870,000)

CONVERTIBLE CORPORATE BONDS - 0.13%

Indonesia - 0.13%

<i>BLT International Corp.</i>	12.000%	02/10/2015	500,000	509,275
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TOTAL CONVERTIBLE CORPORATE BONDS	509,275
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(Amortized Cost \$500,000)

See Notes to Financial Statements.

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Statement of Investments

May 31, 2011 (Unaudited)

	Currency	Rate	Maturity Date	Principal Amount *	Market Value (Expressed in U.S. \$)
CORPORATE BONDS - 30.02%					
Argentina - 0.62%					
Capex SA		10.000%	03/10/2018	\$ 1,279,000	\$ 1,272,349 ⁽⁴⁾
Empresa Distribuidora Y Comercializadora Norte		9.750%	10/25/2022	511,000	523,775 ⁽⁴⁾
Tarjeta Naranja SA		9.000%	01/28/2017	553,000	573,588 ⁽⁴⁾
					2,369,712
Brazil - 2.31%					
Banco Cruzeiro do Sul SA		8.875%	09/22/2020	2,372,000	2,342,587 ⁽⁵⁾
BR Malls International Finance Ltd.		8.500%	01/21/2049	512,000	543,846 ⁽⁴⁾
General Shopping Finance Ltd.		10.000%	11/09/2015	1,341,000	1,414,581 ⁽⁴⁾
Hypermarcas SA		6.500%	04/20/2021	1,387,000	1,390,468 ⁽⁴⁾
Marfrig Holding Europe BV		8.375%	05/09/2018	840,000	832,860 ⁽⁴⁾
Mirabela Nickel Ltd.		8.750%	04/15/2018	297,000	300,712 ⁽⁴⁾
OGX Petroleo e Gas Participacoes SA		8.500%	06/01/2018	1,532,000	1,575,662 ⁽⁴⁾
Virgolino de Oliveira Finance Ltd.		10.500%	01/28/2018	413,000	441,167 ⁽⁵⁾
					8,841,883
China - 1.05%					
Country Garden Holdings Co.		11.125%	02/23/2018	750,000	782,850 ⁽⁴⁾
Hidili Industry International Development Ltd.		8.625%	11/04/2015	404,000	400,465 ⁽⁵⁾
Kaisa Group Holdings Ltd.		13.500%	04/28/2015	1,300,000	1,317,875 ⁽⁵⁾
MIE Holdings Corp.		9.750%	05/12/2016	1,532,000	1,522,502 ⁽⁴⁾
					4,023,692
Colombia - 0.30%					
Emgesa SA ESP	COP	8.750%	01/25/2021	911,000,000	539,328 ⁽⁴⁾
Empresas Publicas de Medellin ESP	COP	8.375%	02/01/2021	1,030,000,000	595,619 ⁽⁴⁾
					1,134,947
Dominican Republic - 1.08%					
Cap Cana SA:		10.000%	04/30/2016	3,182,011	